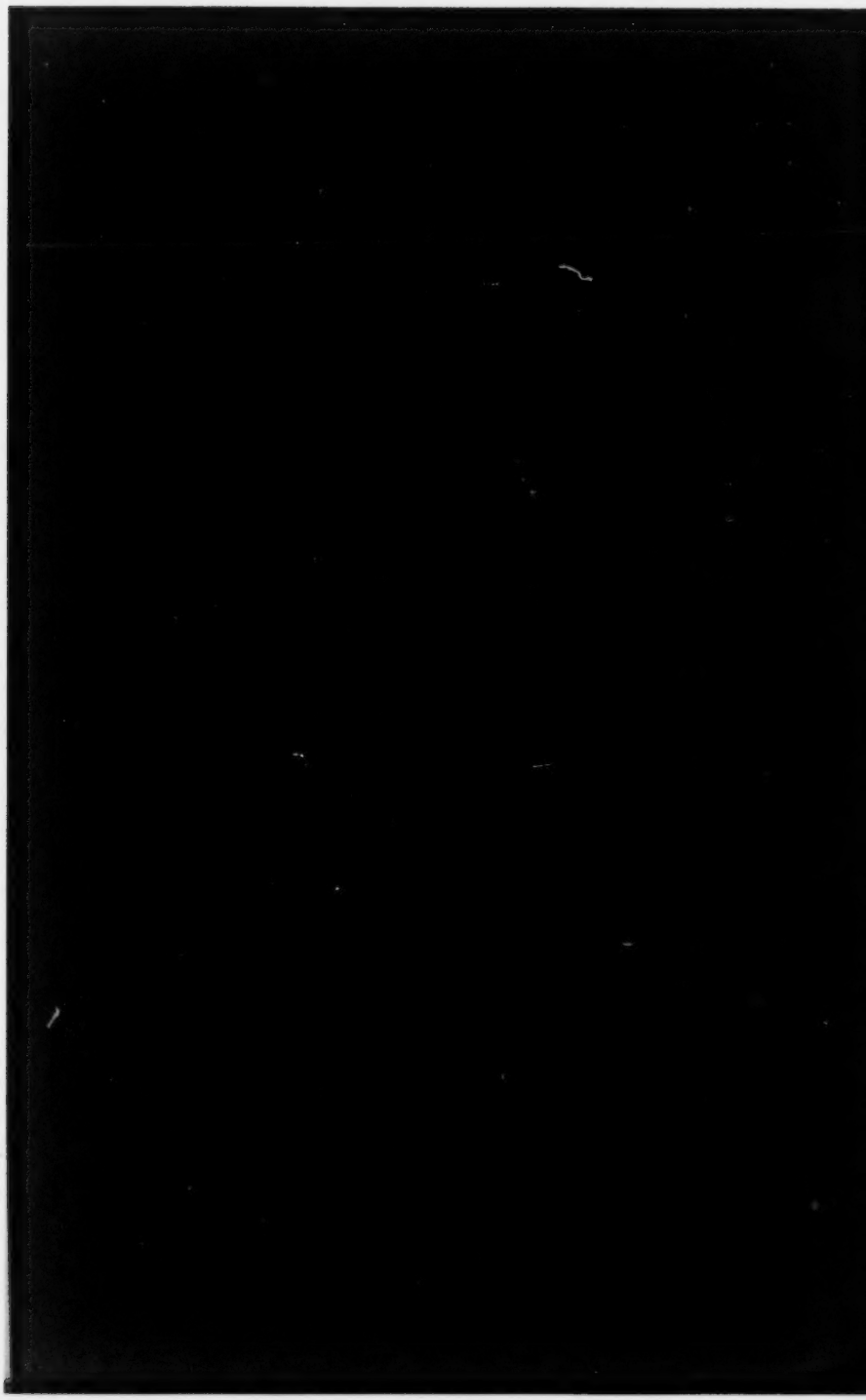

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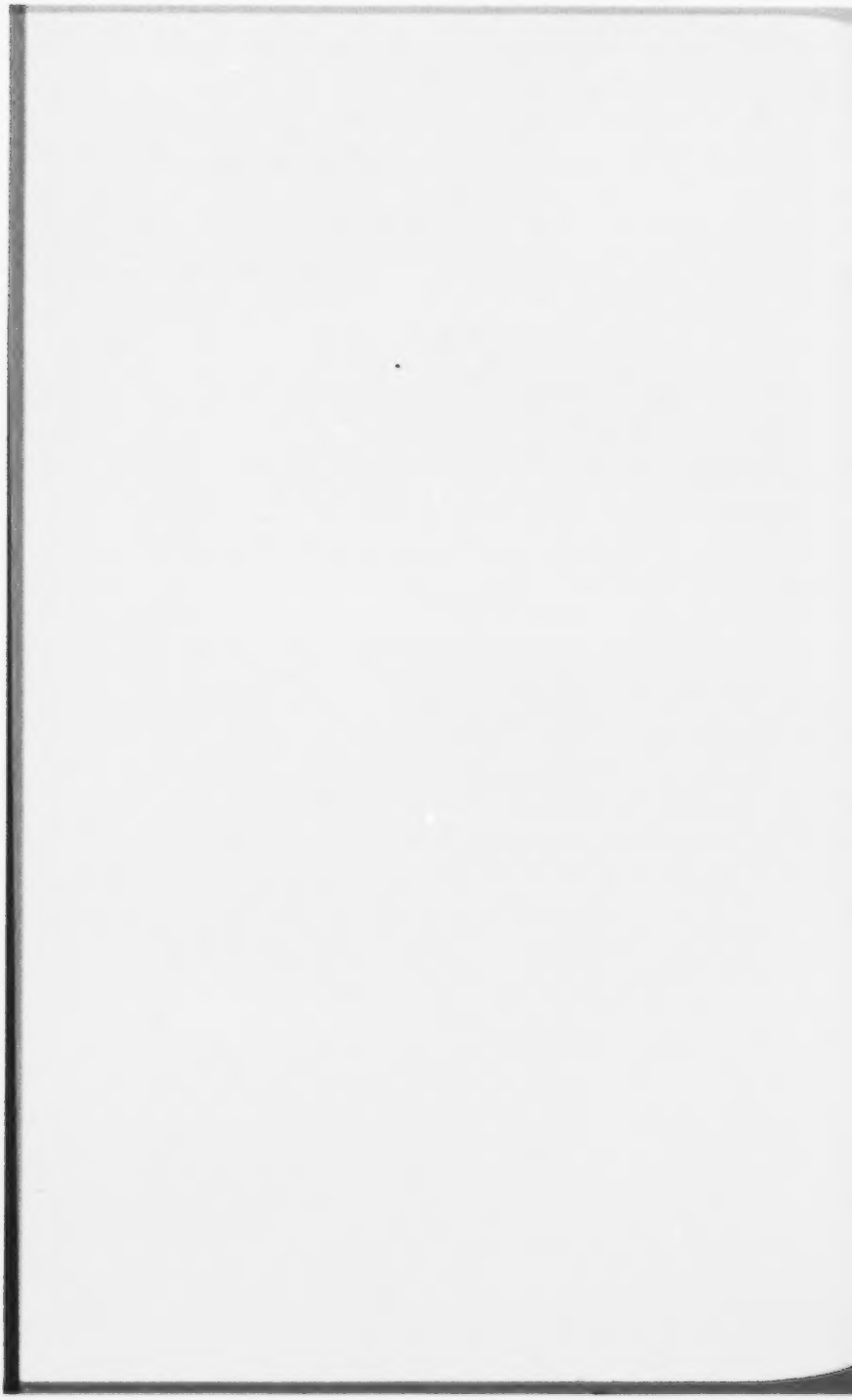

In the Supreme Court of the United States

OCTOBER TERM, 1941

No. 1184

O. O. OWENS, PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE TENTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the Board of Tax Appeals (R. 468–481) in this proceeding is unreported. Two previous opinions of the Board (R. 51–59, 90–101) which related in part to the issues herein are likewise unreported. The opinion of the United States Circuit Court of Appeals for the Tenth Circuit (R. 645–651) is reported in 125 F. (2d) 210.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered January 13, 1942. (R. 652.) Peti-

tion for rehearing, filed February 12, 1942 (R. 655–689), was denied February 26, 1942 (R. 690). The petition for writ of certiorari was filed April 28, 1942. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

Whether the petitioner sustained a deductible loss, or in the alternative incurred a deductible expense, of $75,989.20, in the taxable year 1920. Specifically, the questions are—

1. Whether the expenditure alleged to have been made by the petitioner was a capital outlay, rather than a deductible loss or expense.

2. Whether the item in question was in any event not deductible in 1920 since it was paid in 1922 and since petitioner was on the cash basis of accounting.

3. Whether even if the petitioner kept his books on the accrual basis of accounting, the item was nevertheless not deductible in 1920, since it did not accrue until 1921 or 1922.

STATUTE INVOLVED

Revenue Act of 1918, c. 18, 40 Stat. 1057:

> SEC. 214. (a) That in computing net income there shall be allowed as deductions:
>
> (1) All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including a reasonable allowance for salaries

or other compensation for personal services actually rendered, and including rentals or other payments required to be made as a condition to the continued use or possession, for purposes of the trade or business, of property to which the taxpayer has not taken or is not taking title or in which he has no equity;

* * * * *

(4) Losses sustained during the taxable year and not compensated for by insurance or otherwise, if incurred in trade or business;

(5) Losses sustained during the taxable year and not compensated for by insurance or otherwise, if incurred in any transaction entered into for profit, though not connected with the trade or business; but in the case of a nonresident alien individual only as to such transactions within the United States;

* * * * *

STATEMENT

The sole issue in this case is whether petitioner is entitled to a deduction of $75,988.20 from his gross income for the year 1920, as a loss, or otherwise. That amount represents petitioner's asserted share in certain impounded oil royalties which were relinquished by him and his associates in 1922 to one Martha Jackson, an incompetent, pursuant to an agreement (executed October 22, 1921) which was approved by a court order in 1922. The facts out of which this controversy arose are

complex, but for present purposes they may be summarized as follows:

In 1902 an allotment of land in Oklahoma was made to Barney Thlocco, a full-blooded Creek Indian. It appears, however, that Thlocco had died prior to the allotment, and upon the discovery of oil the United States brought suit in 1913 to cancel the allotment and recover the lands for the benefit of the Creek Nation. Over 200 persons appeared in the litigation as defendants, claiming to be heirs or successors of heirs of Thlocco. A receiver was appointed in 1914, and he leased the lands to an oil company at a specified royalty which was to be paid into court to be accumulated for distribution to those who should ultimately be determined to be entitled thereto. This Court finally held on May 21, 1917, that the United States could not cancel the allotment. *United States* v. *Wildcat,* 244 U. S. 111. There then remained for the lower courts the problem of determining who among the various defendants might be entitled to the land and the impounded royalties. (R. 469–470.)

Among those who asserted claims of heirship were one Saber Jackson, who claimed a life estate by curtesy, and his daughter Martha Jackson, who claimed a fee simple. (R. 470.) In 1916 Saber Jackson had sold his interest to the petitioner herein and two associates. (R. 470.) Moreover, on July 9, 1917, one Parmenter, acting as the guardian of Martha Jackson, contracted

with an agent of the petitioner and his associates to convey her interest in the lands and impounded funds, in consideration of $12,000 cash plus 25 per cent of such of the impounded funds as should ultimately be adjudged to belong to her; the purchasers also undertook to prosecute her claim and to defeat or acquire all adverse claims. (R. 470.) On July 9, 1917, the impounded royalties amounted to $698,836.89. (R. 470.) On February 26, 1918, petitioner and his associates transferred their interests to the lessee oil company, which in turn assumed the obligation of the purchasers to Martha Jackson. On that day the impounded funds amounted to $893,365.94, and the oil company together with an assignee expended $395,480.34 in carrying out those obligations. (R. 470–471.)

As a result of dissatisfaction of the Department of the Interior with the contract of July 9, 1917, in respect of the amounts payable to Martha Jackson, the petitioner and his associates on May 11, 1918, entered into a supplemental contract which provided that she should receive $111,870.74 of the impounded royalties plus one-eighth of the funds that should be accumulated thereafter. (R. 471–472.)

On June 17, 1919, the District Court entered a decree in which it adjudged that Martha Jackson was the sole heir of Thlocco, that she was, on June 9, 1917, the owner of the allotment, subject only to Saber Jackson's curtesy estate, and that

she was also the owner of the impounded royalties. It further decreed that by reason of the conveyances, petitioner and his associates together with their assignees had succeeded to her interest. (R. 472.) Meanwhile, Saber Jackson attempted to intervene, seeking to set aside his 1916 conveyance on the ground of fraud, and Martha Jackson also attempted to intervene through another guardian challenging the validity of her contracts and conveyances on the ground of fraud. On September 9, 1919, the District Court denied both applications for intervention. (R. 472.) An appeal was taken from the rulings of the District Court, and while that appeal was pending, the Secretary of the Interior promulgated an order setting forth that the contract of May 11, 1918, had not been approved by him or the Interior Department, and that Martha Jackson's interest in the impounded funds as of the date of her conveyance was equal to approximately $325,000. (R. 473.) That order was promulgated May 6, 1920, and petitioner and his associates thereafter, on October 22, 1921, entered into a further supplemental agreement with Martha Jackson and the oil company whereby it was agreed that she should receive $308,000 of the impounded funds, an amount computed so as to comply with the order of the Secretary of the Interior. (R. 310–313, 473.) On March 25, 1922, the Circuit Court of Appeals sustained a motion asking for the reform of the District Court's de-

cree in accordance with the terms of that supplementary contract, and remanded the cause with directions that the decree be modified so as to comply with the terms of the contract. (R. 473, 522.) It was thus ordered that $308,000 be paid out of the impounded funds for the use of Martha Jackson. *M'Kinney* v. *Black Panther Oil & Gas Co.*, 280 Fed. 486 (C. C. A. 8th).[1]

In September 1922, $318,261.04 was paid out of the impounded funds for the benefit of Martha Jackson. On February 3, 1923, the Circuit Court of Appeals entered an order adjudicating the rights of Saber Jackson, and on May 29, 1923, the District Court entered a final order, disposing of all matters in controversy. (R. 474.)

The amount ($75,989.20) which petitioner seeks to deduct from his gross income for 1920 represents his allocable share of the additional amount paid to Martha Jackson under the supplemental contract of October 22, 1921, which was ultimately approved.[2]

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[1] On the same day the Circuit Court of Appeals affirmed another judgment of the District Court ruling that one Saley was not an heir of Thlocco. *Saley* v. *Black Panther Oil & Gas Co.*, 280 Fed. 496 (C. C. A. 8th).

[2] The record does not show just how petitioner computed his deduction. It was probably computed roughly as follows: The agreement of May 11, 1918, provided that $111,870.74 of the impounded royalties be paid to Martha Jackson, and the later agreement approved by the Circuit Court of Appeals raised that amount to $308,000. Petitioner stated that he had a three-eighths interest in the enterprise, and the

The Board sustained the Commissioner's determination denying the deduction (R. 481), holding (1) that petitioner, who did not keep any regular books of account, was on the cash basis of accounting and could not deduct in 1920 any amounts in fact paid out in 1922; and (2) that even if he were on the accrual basis, his liability under the new agreement had not become definitely fixed until 1922 with the consequence that it could not be accrued in 1920. (R. 477–481.) The Circuit Court of Appeals affirmed upon still another ground, namely, that in any event, such additional amount was at most expended in the acquisition of a capital asset and was therefore not deductible at all.

ARGUMENT

The peculiar facts of this case do not raise any question calling for further review. There is no conflict, and the decision is correct on any one of the three grounds relied upon below.

1. Assuming, *arguendo,* that the petitioner may be treated as having made the outlay in question, it was plainly no more than a capital expenditure. It represented at most only additional consideration that was paid to acquire Martha Jackson's interest, and was therefore not deductible at all. The decisions cited by the court below on this is-

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amount claimed by him as a deduction is roughly three-eighths of the difference between those two amounts. (R. 477.)

sue (R. 650–651) amply sustain its conclusion, and to those decisions may be added the following: *Brush-Moore Newspapers, Inc.* v. *Commissioner,* 95 F. (2d) 900 (C. C. A. 6th), certiorari denied, 305 U. S. 615; *Colony Coal & Coke Corp.* v. *Commissioner,* 52 F. (2d) 923 (C. C. A. 4th); *Hutchings* v. *Burnet,* 58 F. (2d) 514 (App. D. C.); *Blackwell Oil & Gas Co.* v. *Commissioner,* 60 F. (2d) 257 (C. C. A. 10th); *J. I. Case Co.* v. *United States,* 32 F. Supp. 754 (C. Cls.). There are no decisions to the contrary, notwithstanding petitioner's bald assertion that the decision herein is in conflict with the very cases relied upon by the court.

2. Moreover, the Board found that petitioner was on the cash basis of accounting and that he did not keep any regular books on the accrual basis. (R. 478.) The record fully justifies that conclusion. Accordingly, since the amount in question was not paid to Martha Jackson until 1922, it could not be deducted in 1920 by one on the cash basis.

3. Finally, even if the amount were otherwise deductible and even if petitioner were on the accrual basis, the item did not accrue in 1920. Petitioner claims that the contract giving rise to that additional liability was executed on December 5, 1920. (Pet. 19, Br. 27, 31, 61, 69–89.) But that contract was entered into with one McKinney, an alleged guardian of Martha Jackson, and was not

the contract which formed the basis for the 1922 judgment. (R. 279, 283, 285.) The contract which formed the basis for the judgment was entered into with Martha Jackson's duly appointed guardian, Parmenter, and was executed on October 22, 1921. (R. 310–313.) Accordingly, even if petitioner were on the accrual basis, the liability in question could not have accrued prior to 1921. Petitioner is therefore not entitled to any deduction for 1920.

CONCLUSION

The decision below is correct on any one of at least three theories. There is no conflict. The petition should be denied.

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MAY, 1942.

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